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Jonathan G. Katz
Secretary
Securities and Exchange Commission
450 Fifth Street, N.W.
Washington, D.C. 20549-0609

Re: Retention and Production of E-Mail by Investment Advisers

Dear Mr. Katz:

The Committee on Investment Management Regulation of the Association of the Bar of The City of New York (the "Committee") would like to take this opportunity to request that the Commission provide greater written guidance, through the public rulemaking process, on the obligation of investment advisers to retain and produce e-mail.[1] The Committee is making this request because it has serious concerns about how the Commission and its staff have used the inspection and enforcement process to implement Rule 204-2 under the Investment Advisers Act in relation to e-mail. Rule 204-2 requires advisers to retain certain records, communications, and other types of information, and, over the last several years, the SEC staff has, through the inspection and enforcement process, informally interpreted Rule 204-2 to apply to e-mail. In doing so, however, the Commission and the staff have created ambiguities regarding an adviser's obligations to store and produce e-mail. The intersection of these ambiguous requirements with the incredible growth of business e-mail has raised a host of difficult compliance issues for investment advisers. As Commissioner Atkins noted in a speech very recently, these issues are a

[1] The Committee understands that the staff may be preparing some form of written guidance on this subject. Nonetheless, given the great significance of these issues and the fact that they have not previously been the subject of rulemaking by the Commission, the Committee believes that, as discussed below, the issues of e-mail retention and production should be addressed through the public rulemaking process.

subject of great concern to registered investment advisers.[2] The Committee believes that at least two issues require the immediate attention of the Commission.

First, there is great uncertainty among advisers about how to comply with the retention requirements as they apply to e-mail. Though the staff has acknowledged that advisers need not save e-mail without information required to be retained, the staff has indicated that advisers that do not retain all e-mail must put into place procedures reasonably designed to ensure that required information is retained. Many advisers, however, still feel compelled to keep all e-mail communications for five years for fear that inspectors will either deem the adviser's procedures unreasonable or will insist on absolute certainty that all required records have not been deleted (a negative that would be impossible to prove).[3] Maintaining all of a firm's e-mail for five years, however, is becoming increasingly burdensome due to the explosive growth in the use of e-mail. This difficult situation could be eased by a more formal statement from the Commission stating that reasonable procedures will satisfy an adviser's retention requirement with respect to e-mail and giving guidance as to the types of procedures the Commission would view as reasonable. Further, given how financially burdensome it would be to review every e-mail individually prior to deletion, we submit that the Commission should also make clear that reasonable procedures need not include such an individual review.[4]

Adding to the confusion over what e-mail must be retained is Rule 204-2(a)(7), which requires retention of certain types of written communications. Many in the advisory industry have long interpreted Rule 204-2(a)(7) only to apply to communications between an investment advisory firm and third parties, not to internal documents. It appears, however, that some of the staff in the Office of Compliance Inspections and Examinations have now taken the position that Rule 204-2(a)(7) applies as well to communications among a firm's employees. Given the large volume of e-mail traffic sent among employees every day, complying with the staff position would impose a significant burden on the resources of many advisory firms. In view of the fact that Rule 204-2(a)(7) speaks only of communications "received and . . . sent by" an investment adviser, not of communications within a firm, the Committee believes that the Commission should affirm the long-standing industry interpretation that the Rule applies only to communications with third parties.

The second area in need of immediate Commission attention is that of e-mail production in response to inspection requests. SEC inspectors now routinely request that an adviser promptly produce all firm e-mail, or all e-mail sent or received by certain individuals, in an electronically searchable format. These requests raise two important issues. First, whether the

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[2] Commissioner Paul S. Atkins, "Remarks Before the California '40 Acts Institute" (April 27, 2005).

[3] Indeed, the Committee has learned that, on occasion, SEC examination staff members have taken the position (in contrast to other statements by the staff) that an adviser must keep all employee e-mail regardless of whether it contains Rule 204-2 information. The Committee, however, believes that this position has no support in either the law or the rules.

[4] The Committee further believes that reasonable e-mail retention procedures should permit the deletion of e-mail that has been filtered out of a recipient's e-mailbox by a recognized "spam" or "junk" e-mail filtering program. Regular deletion of junk e-mail would help to lighten the burden of retaining e-mail.

Commission has authority to inspect all adviser records and, second, whether the Commission can require all records to be produced in a specific format.

With respect to the first issue, the SEC has taken the position that Section 204 of the Investment Advisers Act allows it to review any record of an adviser, whether required to be retained by Rule 204-2 or not. Section 204 provides:

> Every investment adviser . . . shall make and keep . . . such records (as defined in Section 3(a)(37) of the [Exchange Act]) . . . as the Commission, by rule, may prescribe . . . . All records (as so defined) of such investment advisers are subject at any time . . . [to] reasonable periodic, special, or other examinations [by the Commission.]

The Committee submits that Section 204 authorizes the Commission to require by rule that investment advisers retain records that it deems necessary to protect investors and to inspect the records it requires investment advisers to retain. If the Commission believes that Rule 204-2 is not broad enough in its scope, it should promulgate new rules. Rulemaking entails a transparent process open to public comment**.** Creating law through the inspection and enforcement process, on the other hand, not only violates the Administrative Procedures Act, but it also subjects investment advisers to ad hoc and varying requests that create expensive uncertainty.

Regardless of whether all records are subject to inspection, or just those that are required to be retained by the Rule, it is clear that only certain records are required to be kept in a particular electronic format. Specifically, Rule 204-2(g) provides that required records maintained electronically must be arranged in a way that permits easy access and location. This requirement, however, does not apply to records that are not required to be retained. Because of the considerable expense that can be incurred in converting saved electronic records from a format that was never intended to be searchable (e.g., back-up storage drives) into a searchable format, the Committee submits that advisory firms may, until required to do otherwise by rule or regulation, produce non-required electronic records to the staff in any format or medium.[5] Nonetheless, in light of staff requests that are apparently outside the strictures of the rules, only Commission action will settle these e-mail production questions with certainty.

The Committee believes that the Commission should act promptly to resolve the issues surrounding the storage and production of e-mail. The growing importance of e-mail to the everyday conduct of business will require investment advisers to dedicate substantial amounts of capital and manpower to implementing the technology necessary to comply with their record retention and production obligations. It is, however, fundamentally unfair to ask these firms to make such large financial commitments while the area is still so rife with ambiguities such as

[5] Similarly, some SEC staff appear to have taken the position that every e-mail that is required to be saved must be saved in electronic format, even though no existing rule requires that to be done. Many advisers have found it more convenient to retain e-mail in paper format.

those described above.[6] The Committee therefore requests that the Commission address these issues through the rulemaking process with its attendant opportunity for public comment.

The Committee would be pleased to answer any questions you might have regarding this letter, and to meet with the staff if that would assist the Commission's efforts.

Very truly yours,

Stuart H. Coleman
Chair

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[6] The Committee notes that the uncertainty surrounding e-mail retention is even greater for the many investment advisers that are also registered broker-dealers. These advisers must not only comply with the Investment Advisers Act and its rules, but they must also satisfy the e-mail retention requirements imposed both by the Securities Exchange Act of 1934 (and its rules) and by the Self-Regulatory Organizations to which these advisers belong (such as the NYSE or the NASD). This tripartite system only compounds the difficulty these advisers face in comprehending their e-mail retention obligations. The Committee therefore believes that the Commission should seek to standardize these requirements such that advisers that are also broker-dealers are not subject to varying e-mail retention regimes.

The Association of the Bar of The City of New York
Committee on Investment Management Regulation

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